

CHAPTER 7

FIELD WORK STANDARDS FOR PERFORMANCE AUDITS

INTRODUCTION

7.1 This chapter prescribes field work standards and provides guidance to auditors conducting performance audits in accordance with generally accepted government auditing standards (GAGAS). The field work standards for performance audits relate to planning the audit, supervising staff, obtaining sufficient, competent, and relevant evidence, and preparing audit documentation.

PLANNING

7.2 The field work standard related to planning for performance audits conducted in accordance with GAGAS is:

Work is to be adequately planned.

7.3 In planning the audit, auditors should define the audit objectives, as well as the scope, and methodology to achieve those objectives. Audit objectives, scope, and methodologies are not determined in isolation. Auditors determine these three elements of the audit plan together, as the considerations in determining each often overlap. Planning is a continuous process throughout the audit. Therefore, auditors should consider the need to make adjustments to the audit objectives, scope, and methodology as work is being completed.

7.4 The objectives are what the audit is intended to accomplish. They identify the audit subjects and performance aspects to be included, as well as the potential finding and reporting elements

that the auditors expect to develop.¹ Audit objectives can be thought of as questions about the program² that auditors seek to answer. (See chapter 2.)

7.5 Scope is the boundary of the audit and should be directly tied to the audit objectives. For example, the scope defines parameters of the audit such as the period of time reviewed, the availability of necessary documentation or records, and the number of locations at which field work will be conducted.

7.6 The methodology comprises the work involved in gathering and analyzing data to achieve the objectives. Audit procedures are the specific steps and tests auditors will carry out to address the audit objectives. Auditors should design the methodology to provide sufficient, competent, and relevant evidence to achieve the objectives of the audit. Methodology includes both the types and extent of audit procedures used to achieve the audit objectives. Auditors may use different methodologies drawn from a wide variety of disciplines.³

7.7 Planning should be documented and should include

- a.** considering the significance of various programs and the needs of potential users of the audit report (see paragraphs 7.8 and 7.9);
- b.** obtaining an understanding of the program to be audited (see paragraph 7.10);

¹See discussion of the elements of a finding in paragraphs 7.45 through 7.48.

²This chapter uses only the term program; however, the concepts presented also apply to audits of organizations, activities, and services.

³If the auditor chooses to apply or use standards or methodologies developed by other professional organizations when performing work under GAGAS, the auditor should also apply the standards in this chapter as appropriate. Even if auditors do not follow such other standards and methodologies, they may still serve as a useful source of guidance to auditors in planning their work under GAGAS. However, if auditors decide to perform their work in accordance with the standards for attestation engagements issued by the AICPA, auditors should apply the additional GAGAS standards for attestation engagements contained in chapter 6.

- c. obtaining an understanding of internal control as it relates to the specific objectives and scope of the audit, (see paragraphs 7.11 through 7.16);
- d. designing the audit methodology and procedures to test compliance with legal and regulatory requirements of the program to be audited that are significant to the specific objectives and scope of the audit (see paragraphs 7.17 through 7.20);
- e. identifying the criteria needed to evaluate matters subject to audit (see paragraph 7.21);
- f. considering the results of previous audits that could affect the current audit objectives (see paragraphs 7.22 and 7.23);
- g. identifying potential sources of data that could be used as audit evidence (see paragraph 7.24);
- h. considering whether the work of other auditors and experts may be used to satisfy some of the auditors' objectives (see paragraphs 7.25 and 7.27);
- i. providing appropriate and sufficient staff and other resources to perform the audit (see paragraph 7.28-7.31);
- j. communicating general information concerning the planning and conduct of the audit to management officials responsible for the program being audited, and others as applicable (see paragraphs 7.32 and 7.33); and
- k. documenting planning decisions (see paragraphs 7.34 through 7.36).

Program Significance

7.8 The significance of a matter is its relative importance to the audit objectives and potential users of the audit report. Auditors should consider the significance of a program or program

component and the potential use that will be made of the audit results or report as they plan a performance audit. Indicators of significance and/or use to consider include

- a. visibility and sensitivity of the program under audit,
- b. newness of the program or changes in its conditions,
- c. role of the audit in providing information that can improve public accountability and decisionmaking, and
- d. level and extent of review or other forms of independent oversight.

7.9 One group of users of the auditors' report is government officials who may have authorized or requested the audit. Another important user of the auditors' report is the entity being audited, which is responsible for acting on the auditors' recommendations. Other potential users of the auditors' report include government legislators or officials (other than those who may have authorized or requested the audit), the media, interest groups, and individual citizens. In addition to an interest in the program, potential users may have an ability to influence the conduct of the program. An awareness of these potential users' interests and influence can help auditors understand why the program operates the way it does. This awareness can also help auditors judge whether possible findings could be significant to various possible users.

Understanding the Program

7.10 Auditors should obtain an understanding of the program to be audited to help assess, among other matters, the significance of possible audit objectives and the feasibility of achieving them. The auditors' understanding may come from knowledge they already have about the program or knowledge they gain from inquiries and observations they make in planning the audit. The extent and breadth of those inquiries and observations will vary among audits based on the audit

objectives, as will the need to understand individual aspects of the program, such as the following.

a. Laws and regulations: Government programs usually are created by law and are subject to more specific laws and regulations than the private sector. For example, laws and regulations usually set forth what is to be done, who is to do it, the purpose to be achieved, the population to be served, and how much can be spent on what. Thus, understanding the laws and the legislative history establishing a program can be essential to understanding the program itself. Obtaining that understanding is also a necessary step in identifying provisions of laws and regulations significant to audit objectives.

b. Purpose and goals: Purpose is the result or effect that is intended or desired from a program's operation. Legislatures usually establish the program purpose when they provide authority for the program. Entity officials may provide more detailed guidance on program purpose to supplement the authorizing legislation. Entity officials are sometimes asked to set goals for program performance and operations, including both outcome and output goals. Auditors may use the stated program purpose and goals as criteria for assessing program performance or may develop additional criteria or best practices to compare the program with.

c. Internal control: Internal control, often referred to as management controls, in the broadest sense includes the plan of organization, methods, and procedures adopted by management to meet its missions goals and objectives. Internal control includes the processes for planning, organizing, directing, and controlling program operations. It includes the systems for measuring, reporting, and monitoring program performance. Internal control also serves as the first line of defense in safeguarding assets and preventing and detecting errors and fraud. Paragraphs 7.11 through 7.16 contain guidance pertaining to internal control.

d. Efforts: Efforts are the amount of resources (in terms of money, material, personnel, and so forth) that are put into a program. These resources may come from within or outside the entity operating the program. Measures of efforts can have a number of dimensions, such as cost,

timing, and quality. Examples of measures of efforts are dollars, employee-hours, and square feet of building space.

e. Program operations: Program operations are the strategies, processes, and activities management uses to convert efforts into outputs. Program operations are subject to internal control.

f. Outputs: Outputs represent the quantity of a good or service produced by a program. For example, an output measure for a job training program could be the number of persons completing training, and an output measure for an aviation safety inspection program could be the number of safety inspections completed.

g. Outcomes: Outcomes are accomplishments or results of programs. For example, an outcome measure for a job training program could be the percentage of trained persons obtaining a job and still in the work place after a specified period of time. Examples of outcome measures for an aviation safety inspection program could be the percentage reduction in significant safety problems found in subsequent inspections and/or the percentage of significant problems deemed corrected in follow-up inspections. Such outcome measures show progress in achieving the stated program purposes of helping unemployable citizens get and keep jobs and improving the safety of aviation operations. Auditors should be aware that outcomes may be influenced by cultural, economic, physical, or technological factors outside the program. Auditors may use approaches drawn from the field of program evaluation to try to isolate the effects of the program from these other influences.

Internal Control

7.11 Auditors should obtain an understanding of the internal control environment, as well as specific internal controls, that are significant to the audit objectives, including internal control over compliance with legal and regulatory requirements, and consider whether the internal controls have been placed in operation. Auditors also need to consider whether any reliance will be placed on internal controls in designing audit procedures. If so, auditors should include

specific tests of the effectiveness of internal control and consider the results in designing audit procedures.⁴ Management is responsible for establishing effective internal control. The lack of administrative continuity in government units because of changes in elected legislative bodies and in administrative organizations increases the need for effective internal control.

7.12 The following classification of internal control is intended to help auditors better understand internal controls and determine their significance to the audit objectives.

- a. Effectiveness and efficiency of program operations:** Controls over program operations include policies and procedures that management has implemented to reasonably ensure that a program meets its objectives and that unintended actions do not result, such as improper payments. Understanding these controls can help auditors understand the program operations that convert efforts to outputs or outcomes.
- b. Validity and reliability of data:** Controls over the validity and reliability of data include policies and procedures that management has implemented to reasonably ensure that valid and reliable data are obtained, maintained, and fairly disclosed in reports. These controls help assure management that it is getting valid and reliable information about whether programs are operating properly on an ongoing basis. Understanding these controls can help auditors (1) assess the risk that the data gathered by the entity may not be valid or reliable and (2) design appropriate tests of the data.
- c. Compliance with applicable laws and regulations:** Controls over compliance with applicable laws and regulations include policies and procedures that management has implemented to reasonably ensure that program implementation is consistent with laws and regulations.

⁴ Refer to internal control guidance developed for the private sector, *Internal Control – Integrated Framework*, published by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The publication, *Standards for Internal Control in the Federal Government* (GAO/AIMD-00-21.3.1, November 1999), which incorporates the relevant guidance developed by COSO, provides definitions and fundamental concepts pertaining to internal control at the federal level and may be useful to other auditors at any level of government. The related *Internal Control Management and Evaluation Tool* (GAO-01-1008G, August 2001), based on the federal internal control standards, provides a systematic, organized, and structured approach to assessing the internal control structure.

Understanding the controls relevant to compliance with those laws and regulations that the auditors have determined are significant can help auditors assess the risk of illegal acts.

7.13 A subset of these categories of internal control is the safeguarding of resources. Controls over the safeguarding of resources include policies and procedures that management has implemented to reasonably prevent or promptly detect unauthorized acquisition, use, or disposition of resources.

7.14 Auditors can obtain an understanding of internal control through inquiries, observations, inspection of documents and records, or review of other auditors' reports. The procedures auditors perform to obtain an understanding of internal control will vary among audits. One factor influencing the extent of these procedures is the auditors' knowledge about internal control gained in prior audits. Also, the need to understand internal control will depend on the particular aspects of the program the auditors consider in setting objectives, scope, and methodology. The following are examples of how the auditors' understanding of internal control can influence the audit plan.

a. Audit objectives: Poorly controlled aspects of a program have a higher risk of failure, so they may be more significant than others in terms of where auditors would want to focus their efforts.

b. Audit scope: Knowledge of the internal control environment and the status of controls in a certain location may lead auditors to target their efforts there.

c. Audit methodology: Effective controls over collecting, summarizing, and reporting data may enable auditors to limit the extent of their direct testing of data validity and reliability. In contrast, evidence suggesting ineffective controls may lead auditors to perform more direct testing of the data, look for data from outside the entity, or develop their own data.

7.15 When internal controls are significant to the audit objectives, auditors should plan to obtain sufficient evidence to support their judgments about those controls.⁵ The following are examples of circumstances where internal controls can be significant to audit objectives.

a. In determining the cause of unsatisfactory performance, that unsatisfactory performance could result from weaknesses in specific internal controls.

b. When assessing the validity and reliability of performance measures developed by the audited entity, effective internal control over collecting, summarizing, and reporting data will help ensure valid and reliable performance measures.

7.16 Internal auditing is an important part of internal control.⁶ When an assessment of internal control is called for, the work of the internal auditors can be used to help provide reasonable assurance that internal controls are functioning properly and to prevent duplication of effort.

Considering Legal, Regulatory, and Other Compliance Requirements

7.17 When laws, regulations, and other compliance requirements such as provisions of contracts or grant agreements are significant to the audit objectives, auditors should design the audit to provide reasonable assurance about compliance with them. This requires determining which laws, regulations, and other compliance requirements are significant to the audit objectives and assessing the risk that significant noncompliance could occur.⁷ Based on that risk assessment, the auditors design and perform procedures to provide reasonable assurance of detecting

⁵The *Standards for Internal Control in the Federal Government* (GAO/AIMD-00-21.3.1, November 1999) is one source of established criteria auditors can use to support their judgments and conclusions about internal control.

⁶Many government entities have these activities identified by other names, such as inspection, appraisal, investigation, organization and methods, or management analysis. These activities assist management by reviewing selected functions.

⁷The term noncompliance includes not only illegal acts resulting from violations of laws and regulations, but also violations of provisions of contracts or grant agreements.

significant instances of noncompliance. (See paragraphs 7.59 through 7.63 for a discussion of evidence indicative of fraud, illegal acts, or other noncompliance.)

7.18 Auditors may find it necessary to work with legal counsel to (1) determine those laws and regulations that are significant to the audit objectives, (2) design tests of compliance with laws and regulations, or (3) evaluate the results of those tests. Auditors also may find it necessary to rely on the work of legal counsel when audit objectives require testing compliance with provisions of contracts or grant agreements.⁸ Depending on the circumstances of the audit, auditors may find it necessary to obtain information on compliance matters from others, such as investigative staff, other audit organizations or government entities that provided assistance to the audited entity, or the applicable law enforcement authority.

7.19 It is not practical to set precise standards for determining if laws, regulations, or other compliance requirements are significant to audit objectives because government programs are subject to many laws, regulations, and other compliance requirements, and audit objectives vary widely. However, auditors may find the following approach helpful in making that determination.

- a.** Reduce each audit objective to questions about specific aspects of the program being audited (that is, purpose and goals, internal control, efforts, program operations, outputs, and outcomes, as discussed in paragraph 7.10).
- b.** Identify laws, regulations, and other compliance requirements that directly relate to specific aspects of the program included in questions that reflect the audit objectives.
- c.** Determine if violations of those laws, regulations, or other compliance requirements could significantly affect the auditors' answers to the questions that relate to the audit objectives. If they could, then those laws, regulations, and other compliance requirements are likely to be significant to the audit objectives.

⁸ Paragraphs 7.25 through 7.27 discuss relying on the work of others.

7.20 In planning tests of compliance with significant laws, regulations, and other compliance requirements, auditors should assess the risk that noncompliance could occur. That risk may be affected by such factors as the complexity of the laws and regulations or their newness. The auditors' assessment of risk includes consideration of whether the entity has controls that are effective in preventing or detecting noncompliance. Management is responsible for establishing effective controls to ensure compliance with laws and regulations, as well as other compliance requirements such as provisions of contracts or grant agreements. If auditors obtain sufficient evidence of the effectiveness of these controls, they can reduce the extent of their tests of compliance.

Criteria

7.21 Criteria are the standards, measures, expectations of what should exist, best practices, or benchmarks against which performance is compared or evaluated. Criteria, one of the elements of a finding, provide a context for understanding the results of the audit. (See paragraphs 7.45 through 7.48 for a discussion on the other elements of a finding.) The audit plan, where possible, should state the criteria to be used. In selecting criteria, auditors have a responsibility to use criteria that are reasonable, attainable, and relevant to the objectives of the performance audit. The following are some examples of possible criteria:

- a.** purpose or goals prescribed by law or regulation or set by management,
- b.** policies and procedures established by management of the audited entity,
- c.** technically developed standards or norms,
- d.** expert opinions,
- e.** prior years' performance,

- f. performance of similar entities,
- g. performance in the private sector, or
- h. best practices of leading organizations.

Considering the Results of Previous Audits

7.22 Auditors should consider the results of previous audits and follow-up on known significant findings and recommendations⁹ that directly relate to the audit objectives of the performance audit. Auditors should also be alert to the status of relevant findings and recommendations identified in other available audits and studies by other organizations as well. For example, an audit report on an entity's computerized information systems may contain significant findings that could relate to the audit if the entity uses such systems to process its accounting or other information the auditors plan on using. In any event, auditors need to make judgments about the extent of follow-up needed and the appropriate disclosure of uncorrected significant findings and recommendations from prior audits that affect the audit objectives.

7.23 Providing continuing attention to significant findings and recommendations is important to ensure that the benefits of audit work are realized. Ultimately, the benefits of audit work occur when audit findings are resolved through meaningful and effective corrective action taken in response to the auditors' findings and recommendations. Officials of the audited entity are responsible for resolving audit findings and recommendations directed to them and for having a process to track their status. If officials of the audited entity do not have such a process, auditors may wish to establish their own process.

⁹ Significant findings and recommendations are those matters that, if not corrected, could affect the results of the auditors' work and users' conclusions about those results.

Identifying Sources of Audit Evidence

7.24 In identifying potential sources of data that could be used as audit evidence, auditors should consider the validity and reliability of these data, including data collected by the audited entity, data generated by the auditors, or data provided by third parties, as well as the sufficiency and relevance of the evidence. (See paragraphs 7.41 through 7.44 for guidance concerning evidence.)

Considering Work of Other Auditors

7.25 Auditors should determine if other auditors have previously done, or are doing, audits of the program or the entity that operates it. Whether other auditors have done performance audits, financial audits, or attestation engagements, the other auditors may be useful sources of information for planning and performing the audit. If other auditors have identified areas that warrant further study, their work may influence the auditors' selection of objectives. The availability of other auditors' work may also influence the selection of methodology, as the auditors may be able to rely on that work to limit the extent of their own testing.

7.26 If auditors intend to rely on the work of other auditors, they should perform procedures regarding the specific work to be relied on that provide a sufficient basis for that reliance. Auditors can obtain evidence concerning the other auditors' qualifications¹⁰ and independence through prior experience, inquiry, and/or review of the other auditors' external quality control review report. Auditors can determine the sufficiency, relevance, and competence of other auditors' evidence by reviewing their report, audit program, or audit documentation, or by performing supplemental tests of the other auditors' work. The nature and extent of evidence needed will depend on the significance of the other auditors' work and on the extent to which the auditors will rely on that work.

¹⁰ Auditors from another country engaged to conduct audits in their country should meet the professional qualifications to practice under that country's laws and regulations or other acceptable standards, such as those issued by the International Organization of Supreme Audit Institutions. Also see the International Federation of Accountants' *International Standards on Auditing*.

7.27 Auditors face similar considerations when using the work of nonauditors (consultants, experts, specialists, and so forth). In addition, auditors should obtain an understanding of the methods and significant assumptions used by the nonauditors. (See paragraph 3.xx for independence considerations when relying on the work of others.)

Staff and Other Resources

7.28 Staff planning should include, among other things,

- a.** assigning staff with the appropriate collective knowledge, skills, and experience for the job,
- b.** assigning an adequate number of staff and supervisors to the audit,
- c.** providing for on-the-job training of staff, and
- d.** engaging specialists when necessary.

7.29 The availability of staff and other resources and the need for specialized skills are important considerations in establishing the objectives, scope, and methodology. For example, limitations on travel funds may preclude auditors from visiting certain critical locations, or lack of expertise in a particular methodology or with computerized information systems may preclude auditors from undertaking certain objectives. Auditors may be able to overcome such limitations by using staff from any existing local field offices of the audit entity or by engaging consultants with the necessary expertise.

7.30 If the use of a specialist is planned, auditors should have sufficient knowledge to

- a.** articulate the objectives required of the specialist,
- b.** evaluate whether the specified procedures will meet auditors' objectives, and

c. evaluate the results of the procedures applied as they relate to other planned audit procedures.

7.31 Auditors without sufficient knowledge to perform the functions listed above may have to engage a consultant for quality control purposes for the areas related to the specialist's work.

Communicating With Management and Others

7.32 Auditors should communicate information about the specific nature of the audit, as well as general information concerning the planning and conduct of the performance audit, to the various parties involved in the audit to help them understand the objectives, time frames, and any data needs. Such parties may include

- a.** the head of the audited entity;
- b.** the audit committee or, in the absence of an audit committee, the board of directors or other equivalent oversight body;
- c.** the individual who possesses a sufficient level of authority and responsibility for the program or activity being audited; and
- d.** the individuals contracting for or requesting audit services, such as contracting officials or legislative members or staff, if applicable.

7.33 Auditors should use their professional judgment to determine the form, content, and frequency of the communication, although written communication is preferred, and should document the communication. Auditors may use an engagement letter, if appropriate, to communicate the information.

Documenting Planning Decisions

7.34 A written audit plan should be prepared for each audit. The form and content of the written audit plan will vary among audits but should include an audit program or project plan, a memorandum, or other appropriate documentation of key decisions about the audit objectives, scope, and methodology and of the auditors' basis for those decisions. It should be updated, as necessary, to reflect any significant changes to the plan made during the audit.

7.35 Documenting the audit plan is an opportunity for the auditors to review the work done in planning the audit to determine whether

- a.** the proposed audit objectives are likely to result in a useful report,
- b.** the proposed audit scope and methodology are adequate to satisfy the audit objectives, and
- c.** sufficient staff and other resources are available to perform the audit and to meet expected time frames for completing the work.

7.36 Written audit plans may include the following.

- a.** Information about the legal authority for the audited program, its history and current objectives, its principal locations, and other background that can help auditors understand and carry out the audit plan.
- b.** Information about the responsibilities of each member of the audit team (such as preparing audit programs, conducting audit work, supervising and reviewing audit work, drafting reports, handling comments from officials of the audited program, and processing the final report), which can help auditors when the work is conducted at several different locations. In these audits, use of comparable audit methods and procedures can help make the data obtained from participating locations comparable.

- c. Audit programs describing procedures to accomplish the audit objectives and providing a systematic basis for assigning work to staff and for summarizing the work performed.
- d. The general format of the audit report and the types of information to be included, which can help auditors focus their field work on the information to be reported.

SUPERVISION

7.37 The second field work standard for performance audits is:

Staff are to be properly supervised.

7.38 Supervision involves directing the efforts of staff assigned to the audit to ensure that the audit objectives are accomplished. Elements of supervision include providing sufficient guidance to staff members, keeping informed of significant problems encountered, reviewing the work performed, and providing effective on-the-job training.

7.39 Supervisors should satisfy themselves that staff members clearly understand what work they are to do, why the work is to be conducted, and what the work is expected to accomplish. With experienced staff, supervisors may outline the scope of the work and leave details to the staff. With a less experienced staff, supervisors may have to specify audit procedures to be performed as well as techniques for gathering and analyzing data.

7.40 The nature of the review of audit work may vary depending on the significance of the work or the experience of the staff. For example, it may be appropriate to have experienced staff review much of the work of other staff with similar experience.

EVIDENCE

7.41 The third field work standard for performance audits is:

Sufficient, competent, and relevant evidence is to be obtained to afford a reasonable basis for the auditors' findings and conclusions.

7.42 A large part of auditors' work on an audit concerns obtaining and evaluating evidence that ultimately supports their judgments and conclusions pertaining to the audit objectives. In evaluating evidence, auditors consider whether they have obtained the evidence necessary to achieve specific audit objectives. When internal control or compliance requirements are significant to the audit objectives, auditors should also collect and evaluate evidence relating to controls or compliance.

7.43 Evidence may be categorized as physical, documentary, testimonial, and analytical. Physical evidence is obtained by auditors' direct inspection or observation of people, property, or events. Such evidence may be documented in memoranda, photographs, drawings, charts, maps, or physical samples. Documentary evidence consists of created information such as letters, contracts, accounting records, invoices, and management information on performance. Testimonial evidence is obtained through inquiries, interviews, or questionnaires. Analytical evidence includes computations, comparisons, separation of information into components, and rational arguments.

7.44 The guidance in the following paragraphs is intended to help auditors judge the quality and quantity of evidence needed to satisfy audit objectives. Paragraphs 7.45 through 7.48 describe the elements of an audit finding. Paragraphs 7.49 through 7.58 provide guidance to help auditors determine what constitutes sufficient, competent, and relevant evidence to support their findings and conclusions.

Audit Findings

7.45 Audit findings often have been regarded as containing the elements of criteria, condition, and effect, plus cause when problems are found. However, the elements needed for a finding depend entirely on the objectives of the audit. Thus, a finding or set of findings is complete to the extent that the audit objectives are satisfied and the report clearly relates those objectives to the finding's elements. Criteria are discussed in paragraph 7.21, and the other elements of a finding--condition, effect, and cause--are discussed in the following paragraphs.

7.46 Condition: Condition is a situation that exists. It has been determined and documented during the audit.

7.47 Effect: Effect has two meanings, which depend on the audit objectives. When the auditors' objectives include identifying the actual or potential consequences of a condition that varies (either positively or negatively) from the criteria identified in the audit, "effect" is a measure of those consequences. Auditors often use effect in this sense to demonstrate the need for corrective action in response to identified problems. When the auditors' objectives include estimating the extent to which a program has caused changes in physical, social, or economic conditions, "effect" is a measure of the impact achieved by the program. Here, effect is the extent to which positive or negative changes in actual physical, social, or economic conditions can be identified and attributed to program operations.

7.48 Cause: Like effect, cause also has two meanings, which depend on the audit objectives. When the auditors' objectives include explaining why a particular type of positive or negative performance identified in the audit occurred, the reasons for that performance are referred to as "cause." Identifying the cause of problems can assist auditors in making constructive recommendations for correction. Because problems can result from a number of plausible factors or multiple causes, the recommendation can be more persuasive if auditors can clearly demonstrate and explain with evidence and reasoning the link between the problems and the factor or factors they identified as the underlying cause. When the auditors' objectives include

estimating the program's effect on changes in physical, social, or economic conditions, they seek evidence of the extent to which the program itself is the "cause" of those changes.

Tests of Evidence

7.49 Evidence should be sufficient, competent, and relevant to support a sound basis for audit findings, conclusions, and recommendations.

a. Evidence should be sufficient to support the auditors' findings. In determining the sufficiency of evidence, auditors should ensure that enough evidence exists to persuade a knowledgeable person of the validity of the findings. When appropriate, statistical methods may be used to establish sufficiency.

b. Evidence is competent if it is consistent with fact (that is, evidence is competent if it is valid and reliable). In assessing the competence of evidence, auditors should consider such factors as whether the evidence is accurate, authoritative, timely, and authentic. When appropriate, auditors may use statistical methods to derive competent evidence.

c. Evidence is relevant if it has a logical, sensible relationship to the issue being addressed.

7.50 The following presumptions are useful in judging the competence of evidence. However, these presumptions are not to be considered sufficient in themselves to determine competence. The amount and kinds of evidence required to support auditors' conclusions should be based on auditors' professional judgment.

a. Evidence obtained when internal controls are effective is more competent than evidence obtained when controls are weak or nonexistent. Auditors should therefore be particularly careful in cases where controls are weak or nonexistent.

- b.** Evidence obtained through the auditors' direct physical examination, observation, computation, and inspection is more competent than evidence obtained indirectly.
- c.** Original documents provide more competent evidence than do copies.
- d.** Testimonial evidence obtained under conditions where persons may speak freely is more competent than testimonial evidence obtained under compromising conditions (for example, where the persons may be intimidated).
- e.** Testimonial evidence obtained from an individual who is not biased or has complete knowledge about the area is more competent than testimonial evidence obtained from an individual who is biased or has only partial knowledge about the area.
- f.** Evidence obtained from a credible third party may in some cases be more competent than that secured from management or other officials of the audited entity.

7.51 Auditors may find it useful to obtain written representations concerning the competence of certain evidence from officials of the audited entity. Written representations ordinarily confirm oral representations given to auditors, indicate and document the continuing appropriateness of such representations, and reduce the possibility of misunderstanding concerning the matters that are the subject of the representations. Written representations can take several forms, including having entity management sign summary documents prepared by the auditors.

7.52 The auditors' approach to determining the sufficiency, competence, and relevance of evidence depends on the source of the information that constitutes the evidence. Information sources include original data gathered by auditors and existing data gathered by either management or a third party. Data from any of these sources may be obtained from computer-based systems.

7.53 Data gathered by auditors: Data gathered by auditors include the auditors' own observations and measurements. Among the methods for gathering this type of data are questionnaires, structured interviews, direct observations, and computations. The design of these methods and the skill of the auditors applying them are the keys to ensuring that these data constitute sufficient, competent, and relevant evidence. When these methods are applied to determine cause, auditors are concerned with eliminating rival explanations.

7.54 Data gathered by management: Auditors can use data gathered by management as part of their evidence. However, auditors should determine the validity and reliability of these data that are significant to the audit objectives and may do so by direct tests of the data. Auditors can reduce the direct tests of the data if they test the effectiveness of the entity's internal controls over the validity and reliability of the data, and these tests support the conclusion that the controls are effective. The nature and extent of testing of the data will depend on the significance of the data to support auditors' findings.

7.55 Data gathered by third parties: The auditors' evidence may also include data gathered by third parties. In some cases, these data may have been audited by others, or the auditors may be able to audit the data themselves. In other cases, however, it will not be practical to obtain evidence of the data's validity and reliability. How the use of unaudited third-party data affects the auditors' report depends on the data's significance to the auditors' findings. For example, in some circumstances, auditors may use unaudited data to provide background information; however, the use of such unaudited data would generally not be appropriate to support audit findings and conclusions.

7.56 Validity and reliability of data from computer-based systems: Auditors should obtain sufficient, competent, and relevant evidence that computer-processed data are valid and reliable when those data are significant to the auditors' findings. This work is necessary regardless of whether the data are provided to auditors or auditors independently extract them.¹¹ Auditors

¹¹When computer-processed data are used by the auditor, or included in the report, for background or informational purposes and are not significant to the auditors' findings, citing the source of the data and stating that they were not verified will satisfy the reporting standards for accuracy and completeness set forth in this statement.

should determine if other auditors have worked to establish the validity and reliability of the data or the effectiveness of the controls over the system that produced the data. If the results of such work is current, auditors may be able to rely on that work. (See paragraphs 7.25 through 7.27 for requirements when relying on the work of others.) Auditors may also determine the validity and reliability of computer-processed data by direct tests of the data.

7.57 Auditors can reduce the direct tests of the data if they test the effectiveness of general and application controls over computer-processed data, and these tests support the conclusion that the controls are effective. If auditors determine that internal controls over data which are significantly dependent upon computerized information systems are not effective or if auditors do not plan to test the effectiveness of such controls, auditors should include audit documentation regarding the basis for that conclusion by addressing (1) the reasons why the design or operation of the controls is ineffective, or (2) the reasons why it is inefficient to test the controls. In such circumstances, auditors should also include audit documentation regarding their reasons for concluding that the planned audit procedures are effectively designed to achieve specific audit objectives. This documentation should address

- a.** the rationale for determining the types and extent of planned audit procedures;
- b.** the kinds and competence of available evidence produced outside a computerized information system; and
- c.** the effect on the audit report if the evidence gathered during the audit does not allow the auditors to achieve audit objectives.

7.58 When the auditors' tests of data disclose errors in the data, or when they are unable to obtain sufficient, competent, and relevant evidence about the validity and reliability of the data, they may find it necessary to

- a. seek evidence from other sources,
- b. redefine the audit's objectives to eliminate the need to use the data, or
- c. use the data, but clearly indicate in their report the data's limitations and refrain from making unwarranted conclusions or recommendations.

Evidence Indicative of Fraud, Illegal Acts,
Or Other Noncompliance

7.59 Auditors should be alert to situations or transactions that could be indicative of fraud, illegal acts (violations of laws and regulations), or other noncompliance (violations of other compliance requirements such as provisions of contracts or grant agreements). When information comes to the auditors' attention (through audit procedures, allegations received through fraud hotlines, or other means) indicating that fraud, illegal acts, or other noncompliance may have occurred, auditors should consider whether the possible fraud, illegal acts, or other noncompliance could significantly affect the audit results. If they could, the auditors should extend the audit steps and procedures, as necessary, (1) to determine if fraud, illegal acts, or other noncompliance are likely to have occurred and (2) if so, to determine their effect on the audit results.

7.60 Auditors' training, experience, and understanding of the program being audited may provide a basis for recognizing that some acts coming to their attention may be indicative of fraud, illegal acts, or other noncompliance. Whether an act is, in fact, illegal is a determination to be made through the judicial or other adjudicative system and is beyond auditors' professional expertise and responsibility. However, auditors are responsible for being aware of vulnerabilities to fraud, illegal acts, or other noncompliance associated with the area being audited in order to be able to identify indications that fraud, illegal acts, or other noncompliance may have occurred. In some circumstances, conditions such as the following might indicate a heightened risk of fraud, illegal acts, or other noncompliance:

- a.** weak management which fails to enforce existing internal control or to provide adequate oversight over the control process;
- b.** inadequate separation of duties, especially those that relate to controlling and safeguarding resources;
- c.** transactions that are out of the ordinary and are not satisfactorily explained, such as unexplained adjustments in inventories or other resources;
- d.** instances when employees of the audited entity refuse to take vacations or accept promotions;
- e.** missing or altered documents, or unexplained delays in providing information;
- f.** false or misleading information; or
- g.** history of impropriety, such as past audits or investigations with findings of questionable or criminal activity.

7.61 Auditors should exercise professional judgment in pursuing indications of possible fraud, illegal acts, or other noncompliance so as not to interfere with potential investigations, legal proceedings, or both. Under some circumstances, laws, regulations, or policies require auditors to report indications of certain types of illegal acts to law enforcement or investigatory authorities before extending audit steps and procedures. Auditors may also be required to withdraw from or defer further work on the audit or a portion of the audit in order not to interfere with an investigation.

7.62 An audit made in accordance with these standards provides reasonable assurance of detecting fraud, illegal acts, or other noncompliance that could significantly affect the audit results; it does not guarantee the discovery of fraud, illegal acts, or other noncompliance. Nor

does the subsequent discovery of such acts committed during the audit period necessarily mean that the auditors' performance was inadequate, provided the audit was made in accordance with these standards.

7.63 Abuse is distinct from illegal acts and other noncompliance. When abuse occurs, no law, regulation, contract provision, or grant agreement is violated. Rather, the conduct of a government program falls far short of societal expectations for prudent program management. Auditors should be alert to situations or transactions that could be indicative of abuse. When information comes to the auditors' attention (through audit procedures, allegations received through a fraud hotline, or other means) indicating that abuse may have occurred, auditors should consider whether the possible abuse could significantly affect the audit results. If it could, the auditors should extend the audit steps and procedures, as necessary, (1) to determine if the abuse occurred and (2) if so, to determine its effect on the audit results. However, because the determination of abuse is so subjective, auditors are not expected to provide reasonable assurance of detecting it.

AUDIT DOCUMENTATION

7.64 The fourth field work standard for performance audits is:

Auditors should prepare and maintain audit documentation. Audit documentation should contain sufficient information to enable an experienced reviewer, who has had no previous connection with the audit, to ascertain from the audit documentation the evidence that supports the auditors' significant judgments and conclusions. Audit documentation that supports significant findings, conclusions, and recommendations should be complete before auditors issue their report.

7.65 The form and content of audit documentation should be designed to meet the circumstances of the particular audit. The information contained in audit documentation constitutes the

principal record of the work that the auditors have performed and the conclusions that the auditors have reached. The quantity, type, and content of audit documentation is a matter of the auditors' professional judgment.

7.66 Audit documentation serves three main purposes: (1) to provide the principal support for the auditors' report, (2) to aid auditors in conducting and supervising the audit, and (3) to allow for the review of audit quality. This third purpose is important because audits done in accordance with GAGAS often are subject to review by other auditors and by oversight officials. Audit documentation allows for the review of audit quality by providing the reviewer documentation, either in written or electronic formats, of the evidence supporting the auditors' significant judgments and conclusions.

7.67 Audit organizations should establish reasonable policies and procedures for the safe custody and retention of audit documentation for a time sufficient to satisfy legal and administrative requirements. If audit documentation is only retained electronically, the audit organization should ensure that the electronic documentation is capable of being accessed throughout the specified retention period established for audit documentation and is safeguarded through sound computer security.

7.68 Audit documentation should contain

- a.** the objectives, scope, and methodology, including sampling and other selection criteria used;
- b.** documentation of the auditors' determination that certain standards do not apply or that an applicable standard was not followed, the reasons therefore, and the known effect that not following the standard had, or could have, on the audit;

c. documentation of the work performed to support significant judgments and conclusions, including descriptions of transactions and records examined that would enable an experienced reviewer to examine the same transactions and records;¹² and

d. evidence of supervisory review of the work performed.

7.69 Underlying GAGAS audits is that federal, state, and local governments and other organizations cooperate in auditing programs of common interest so that the auditors may use others' work and avoid duplicate audit efforts. In addition, audits performed in accordance with GAGAS are subject to quality control and assurance reviews. Auditors should make arrangements to make audit documentation available, upon request, in a timely manner to other auditors or reviewers. Contractual arrangements for GAGAS audits should provide for full and timely access to audit documentation to facilitate reliance by other auditors on the auditors' work, as well as reviews of audit quality control and assurance.

¹² The nature of this documentation will vary with the nature of the work performed. For example, when this work includes examination of management's records, the audit documentation should describe those records so that an experienced reviewer would be able to examine those same records. Auditors may meet this requirement by listing file numbers, case numbers, or other means of identifying specific documents they examined. They are not required to include in the audit documentation copies of documents they examined, nor are they required to list detailed information from those documents.